The Nigerian

First Published: May 1980

Banker

Journal of The Chartered Institute of Bankers of Nigeria, July - September, 2016. ISSN 0197-6679 N500.00

BREXIT and its Implications on the Nigerian Banking Industry

- Dynamics of the Nigerian Foreign Exchange Market
- Change and Innovation the Nigerian Banking Industry: An Agenda for Research

THE BANKERS CREED

Hugh McCulloch's Advice to Bankers of 1863

(Hugh McCulloch (1808 – 1895) was an American Banker who helped launch the American National Banking System and was Secretary of the Treasury during the civil war and reconstruction)

- Let no loans be made that are not secured beyond a reasonable contingency. Do nothing to foster and encourage speculation. Make your loans on as short term as the business of your customers will permit, and insist upon the payment of all paper at maturity, no matter whether you need the money or not. Give credit facilities only to legitimate and prudent transactions. Never renew a note merely because you may not know where to place the money with equal advantage if the note is paid.

- Distribute your loans rather than concentrate them in a few hands. Large loans to a single individual or firm, although sometimes proper and necessary, are generally injudicious, and frequently unsafe. Large borrowers are apt to control the bank; and when this is the relation between a bank and its customers, it is not difficult to decide which in the end will suffer. Every dollar that a bank loans above its capital and surplus it owes for, and its managers are therefore under the strongest obligations to its creditors, as well as to it stockholders, to keep its loans under its control.

- Treat your customers liberally, bearing in mind the fact that bank prospers as its customers prosper, but never permit them to dictate your policy.

- If you have reasons to distrust the integrity of a customer, close his account. Never deal with a rascal under the impression that you can prevent him from cheating you. The risk in such cases is greater than the profits.

- Pay your officers such salaries as will enable them to live comfortably and respectably without stealing; and require of them their entire services. If an officer lives beyond his income, dismiss him; even if his excess of expenditures can be explained consistently with his integrity, still dismiss him. Extravagance, if not a crime, very naturally leads to crime. A man cannot be a safe officer of a bank who spends more than he earns.

- The capital of a bank should be a reality, not fiction; and it should be owned by those who have money to lend, and not by borrowers.

- Pursue a straightforward, upright, legitimate banking business. Never be tempted by the prospect of large returns to do anything but what may be properly done under the National Currency Act. "Splendid financiering" is not legitimate banking, and "splendid financiers" in banking are generally either humbugs or rascals.

THE CHARTERED INSTITUTE OF BANKERS OF NIGERIA

PC 19, Adeola Hopewell Street, Victoria Island, Lagos.

www.cibng.org cibnigeria cibnigeria cibnigeria cibngorg theCIBN cibnigeria

GUIDELINES FOR SUBMISSION OF ARTICLES FOR PUBLICATION IN THE NIGERIAN BANKER

1. The Nigerian Banker Journal welcomes original scholarly research articles from practising professionals, academics, financial consultants/analysts, book reviewers, researchers and policy review analysts, etc in the area of banking and related subjects.

2. Submission of an article for publication in The Nigerian Banker Journal presupposes that the article has never been previously published, nor is it being concurrently submitted for publication elsewhere.

3. Articles should be typed double spaced on A4 size paper and should not exceed 15 pages, bibliography and footnotes inclusive. Long articles should be divided into logical parts so that they can be published in parts, if found publishable.

4. Articles previously presented at Seminars/Workshops/Conferences/Lectures etc may be adopted for publication in The Nigerian Banker Journal provided it is acknowledged at the bottom of the cover page of the article, e.g. "The original version of this article was presented at a seminar on ………………… organised by … … … … … … … … … … … on …………………………..

5. The cover page should contain the following information:
Title of Article
Name of Author(s) (Degrees optional)
Brief bio-data of the Author at the bottom page e.g. XXX is a Senior Lecturer at …… University; or XXX, Financial Analyst, Research Department, ABC International Plc.

6. Text references should be cited in the text as follows: Author's last name, publication year and page e.g. (Alawode A. C., 2002, Pg 30)

7. Full references using the Harvard method should be listed alphabetically at the end of the text as follows: Alawode, A. C., (2002), Federalism and National Building; The Nigerian Banker, Vol. 1 No. 1, June, Lagos.

8. Footnotes should be avoided.

9. Check tables and figures (rows, columns and totals) properly. Explanatory paragraphs should be as near as possible to the relevant tables and figures, which should be appropriately numbered.

10. Only articles that are of high quality in content and relevance may be published. Unpublished articles may not be returned to their authors.

11. One hard copy of the article in addition to soft copy are to be sent by writers. Articles sent without a soft copy may be delayed or not published.

12. Articles lost in transit are the responsibility of the author(s).

13. All articles are the opinions of the authors, neither the Research, Strategy and Advocacy Committee nor the CIBN and its officials are liable thereon.

Further correspondence should be addressed to:

The Editor, The Nigerian Banker

The Chartered Institute of Bankers of Nigeria, PC 19, Adeola Hopewell Street

P O Box 72273, Victoria Island, Lagos

Tel. 01-4617924, 4610655 **Website**: www.cibng.org **E-mail:**cibn@cibng.org

Contents

Editorial Team

The Nigerian Banker
(ISSN:0189-6679)

Published by
The Chartered Institute of Bankers of Nigeria

Letters to the Editor should be sent to:
The Nigerian Banker
Bankers House
PC 19, Adeola Hopewell Street
P.O. Box 72273
Victoria Island, Lagos, Nigeria
Tel: 01-4617924, 01-4610655
E-mail: cibn@cibng.org

Graphic Design
Shegun Shokunbi

Printed by
The CIBN Press Ltd

Printed by
The CIBN Press Limited
7, Turton Street, Sabo-Yaba, Lagos.
E-Mail: cibnpress@yahoo.com

The Governing Council

(May 2016 - May 2018)

Office Holders

Professor Segun Ajibola, Ph.D, FCIB	-	President/Chairman of Council
Uche M. Olowu, Ph.D, FCIB	-	1st Vice President
Mr. Bayo Williams Olugbemi, FCIB	-	2nd Vice President
Mr. Ken Opara, FCIB	-	National Treasurer

Rep. of Body of Past Presidents

Dr. Segun Aina, OFR, FCIB
Otunba (Mrs.) Abosede Adebola Osibogun, FCIB

Other Elected Members

Mr. Dele Alabi , FCIB
Mr. Abdulrahman Yinusa, FCIB
Mrs. Tinuola Thompson-Ajayi, FCIB
Mrs. Ibiye Ekong, HCIB
Mrs. Mojisola Adebisi Bakare-Asieru, HCIB
Gabriel Okenwa, Ph.D, MON, ACIB

Branch Representatives

Sir Steve Nwadiuko, FCIB
Mrs. Silifat Taiwo Ige, FCIB
Barrister Adefisayo Martins, ACIB
Mr. Bestman Azebi, FCIB
Alhaji Muhammad Ladan Musa
Innocent Okwuosa, Ph.D, ACIB

Bank Representatives

Mr. Oladipo Balogun, FCIB	-	First City Monument Bank Plc
Mrs. Bola Adesola, FCIB	-	Standard Chartered Bank Ltd
Mr. Ifie Sekibo, HCIB	-	Heritage Bank Ltd
Mr. Herbert Wigwe, HCIB	-	Access Bank Plc
Mr. Rilwan N. Belo-Osagie	-	FSDH Merchant Bank Ltd
Mr. Nnamdi Okonkwo, HCIB	-	Fidelity Bank Plc

Regulatory Institutional Representatives

Alh. Umaru Ibrahim, mni, FCIB	-	Managing Director/ Chief Executive, NDIC
Mrs. Agnes O. Martins, HCIB	-	Director, Banking Supervision, CBN
Mrs. Rakiya Bakari-Girei	-	Federal Ministry of Finance

Academic Institutional Representatives

Mallam Adamu Adamu	-	Federal Ministry of Education
Prof. Adamu A. Rasheed	-	National Universities Commission
Dr. Masa'udu Adamu Kazaure, mni	-	National Board for Technical Education

Sectoral Associations' Representatives

Dr. Femi Johnson, HCIB	-	Mortgage Banking Association of Nigeria
Mr. Valentine Whensu, MCIB, FCIB	-	National Association of Microfinance Banks

Executive Management

Mr. 'Seye Awojobi, FCIB	-	Registrar/Chief Executive
Mr. Segun Shonubi	-	Group Head, Membership Services Division
Mr. Akin Morakinyo	-	Group Head, Capacity Building & Certification Division
Mrs. Rukayat Yusuf	-	Group Head, Learning and Development Division/CIBNCFS
Mr. Festus Anyanwu, FCIB	-	Group Head, Ethics and Professionalism Division
Mr. Babatunde Apena	-	Group Head, CCPD & E-Learning Division
Mr. Ernest Obasa	-	Ag. Group Head, Finance and Corporate Services Division

From The
Editor's Desk

In the June 2016 referendum on European Union (EU) membership, the United Kingdom (UK) voted to withdraw from the EU. This decision aroused the interests of countries in the world due primarily to the central position of the United Kingdom as the financial hub for most economies. Although the decision to leave the Union by the UK could only take effect at least two years after the announcement – based on the Article 50 of the Treaty on European Union of EU member states – the result of the vote and its implications have continued to occupy a front position in global debates.

On the home front, several projections have been made on the possible impact of BREXIT on the Nigerian economy. While some analysts have a positive outlook others take a more conservative approach in their submissions. The CIBN Centre for Financial Studies (CIBNCFS), a subsidiary of The Chartered Institute of Bankers of Nigeria, blazed the trail in this debate by organizing a Session on BREXIT and its implications for the economy in general and the banking and finance industry in particular. The Centre regularly organizes knowledge events to discuss topical issues bearing on the economy and the banking and finance industry. The outcome of the Session on BREXIT organized by the Centre on July 1, 2016 forms part of the well-researched articles in this edition of the Journal.

This Edition has also critically examined the dynamics of businesses under the newly introduced flexible/floating exchange rate regime in the country. The Communique of the CIBNCFS' Session on Business Dynamics Under a Flexible Exchange Rate Regime is published here as part of the Institute's advocacy role in the industry. While the country has experimented with different regimes with some measures of success, it became expedient for the Central Bank of Nigeria to put in place a regime that would allow market forces to fix the price. Gabriel Udendeh, Ph.D, FCIB in his paper titled Dynamics of the Nigerian Foreign Exchange Market thoroughly examines the management of Forex and foreign exchange potentials in Nigeria as well as the likely challenges of floating exchange rate regime for Nigeria.

The regulatory and innovative developments in the banking and finance industry were extensively analyzed by I. K. Muo, Ph.D, FCIB in his paper titled Policy Changes and Innovation in the Nigerian Banking Industry: An Agenda for Research. The paper availed us a detailed historical background of the banking industry and the developments responsible for the current structure. The paper also discussed the relationship between innovation and business turnover. Through a detailed review of literature, the Author was able to establish the fact that Nigerian banks have become very innovative, especially since the emergence of new generation banks and increased competitiveness, sequel to the advent of SAP in 1986.

The Editorial Board of The Nigerian Banker felicitates with Mr. Phillips Oduoza, FCIB, Former Managing Director/Chief Executive Officer, United Bank for Africa Plc (UBA), for a successful banking career and for delivering the Institute's 4th Valedictory Lecture on Friday, July 22, 2016. We are also proud of and identify with our members who recently bagged their Doctorate Degrees from different institutions of higher learning.

Rukayat Yusuf

BREXIT and its Implications on the Nigerian Banking Industry

Moses K. Tule
Director, Monetary Policy Department, Central Bank of Nigeria

1.0 Introduction

In a landmark Referendum, the British people voted on June 23, 2016, with a decision for the United Kingdom (UK) to exit the European Union (EU), ending years of intensive debates and arguments for and against the UK's continued membership in the European Union. While the vote itself was well anticipated, the outcome was highly unexpected as immediate and significant reverberations were observed across the financial markets. This unprecedented development will undoubtedly significantly impact the economic, financial, social and political landscape of the United Kingdom, the European community and the rest of the world.

These issues are significant to the Nigerian banking and financial system, given the intense exposure and integration to British and European financial markets, which are largely considered a part of the World's financial epicenters. This is especially significant, given that Brexit (a term coined from the words “Britain” and “exit,” is the nickname for a British exit of the European Union) has coincided with a period of strain in the Nigerian financial sector due to fragility of internal and external macroeconomic fundamentals. While the effects of the UK's decision to exit the EU - the 'Post-Brexit Effect' - are highly anticipated, (the final exit is expected to last at least two years, if Britain eventually activates Article 50 of the Lisbon Treaty), an accurate prediction of the impact on domestic and external markets is difficult to ascertain. Nevertheless, tentative projections about the structure of expected effects that Brexit portends for the Nigerian economy on many fronts are possible. The purpose of this brief is to highlight the key issues in the Brexit question as a precursor to identifying the broad implications for the Nigerian economy and the Nigerian banking system.

Following this introduction, the rest of the paper proceeds as follows: section two provides a historical overview of UK relations with the EU, and section three evaluates the possible scenarios for Post-Brexit UK trade relations with the remaining EU members and the rest of the world. Section four presents the prospects and challenges the UK's exit from the European Union portends for the economy and the banking industry in Nigeria, while section five concludes.

2.0 The United Kingdom and the European Union

The United Kingdom is a political union of four countries; England, Scotland, Wales and Northern Ireland. The political union is a parliamentary democracy of equals, with each country headed by a First Minister and the entire Union headed by a Prime Minister - the Head of Government. The Queen of England is the overall Ceremonial Head of the political union, having jurisdiction over all machineries of government in all four countries.

The conception of the EU was a consequence of the devastating World Wars of the first half of the 20th century where economic and political harmony between France and Germany - adversaries at the time - was crucial to establishing a lasting global peace and obviating likely recurrences of hostility between the nations. French Foreign Minister Robert SCHUMAN, in 1950, proposed coal and steel industries of Western Europe be integrated as a first step towards the ultimate goal of a union of countries across Europe. In the following year, six members - West Germany, Belgium, Italy, France, Luxembourg, and the Netherlands - signed the Treaty of Paris that set up the European Coal and Steel Community (ECSC).

On 1 January 1999, the Euro was launched as a new currency in the global money markets

Following the tremendous success of this initiative, the Treaties of Rome established the European Atomic Energy Community (Euratom) and the European Economic Community (EEC) in 1957. Member states agreed to the elimination of internal trade barriers by forming a common, single market. The institutions of ECSC, Euratom and EEC were formally merged into the European Community (EC) in 1967, giving birth to a single Commission, Council of Ministers, and the European Parliament.

In 1973, the European Community membership expanded as Denmark, Ireland, and the United Kingdom joined the Community, followed by further expansion with Greece joining in 1981 and Spain and Portugal in 1986 bringing the total EU Membership to 12 countries at the time. In 1992, further integration, heralded by the signing of the Maastricht Treaty, created the European Union. The treaty entrenched further forms of cooperation in foreign and defence policy, judicial and internal affairs, and in the creation of an economic and monetary union - including a common currency. In 1995, Austria, Finland, and Sweden joined the EU, raising the total membership to 15.

On 1 January 1999, the Euro was launched as a new currency in the global money markets; becoming the unit of exchange for 12 euro-area countries, with the exception of the United Kingdom, Sweden, and Denmark. By 2002, the Euro banknotes and coins became the legal tender for citizens of the 12 euro-area countries. Cyprus, Estonia, Hungary, the Czech Republic, Latvia, Lithuania, Poland, Malta, Slovakia and Slovenia, joined the EU, bringing membership of the Union to 25. In 2007 Bulgaria and Romania joined, bringing the current membership to 27, following which the union reached its current size of 28 member countries with the accession of Croatia on July 1, 2013.

The history of the UK's dealings with the European Union has been dogged by euro-skepticism from the onset. The United Kingdom has always preferred a free trade zone arrangement to a customs union, seeking greater flexibility in direct negotiations of the terms of trade relations with its colonies and the USA, rather than functioning within established common institutions of the EU. The skepticism of Britain towards European Union membership was reflected as the first application for membership was no earlier than 1963. While Britain gained membership of the Union in 1973, it almost immediately contemplated leaving in 1975 via a similar referendum, although with a 67% majority electing to remain.

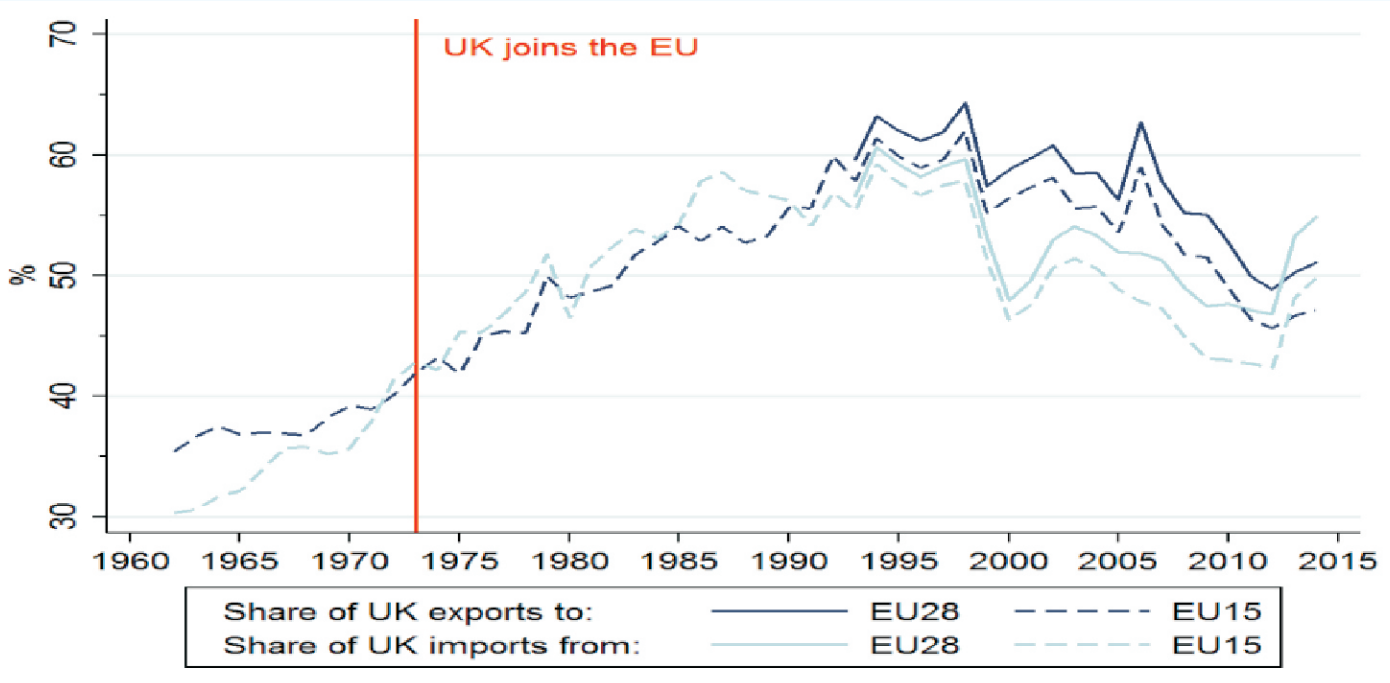
In 1984, The UK Prime Minister, Margaret Thatcher, negotiated a reduction in Britain's contribution to the EU budget. The rebate reduced Britain's EU budget contribution from more than 20 per cent of the total in the '80s to about 15 per cent. Prime Minister Tony Blair, a pro-European Union activist, worked to rebuild ties with the rest of Europe during his tenure. David Cameron, in 2011, became the first UK Prime Minister to veto an EU treaty, and in 2013, highlighted the challenges confronting Europe and promised to renegotiate the terms of UK membership of the EU if his Party were to win the general elections.

The economic crisis plaguing the EU, bailout of distressed member countries, influx of Eastern Europeans into the UK, and the hardline stance of the ruling Party, exacerbated agitations to exit the EU. In May 2015, after winning the elections and in an effort to accommodate the leave EU agitators within his party, the British Prime Minister renegotiated the UK-EU relationship on issues such as changes in welfare payments to migrants, financial safety nets and easier ways for Britain to obviate EU regulations. In February 2016, Cameron, in fulfillment of his campaign promise, announced the results of those negotiations, and set June 23 as the date of the referendum. The final votes in the referendum favored the UK leaving the EU by 52% for leave EU and 48 percent for remain in EU.

Summary statistics indicate the EU as the major trading partner to the UK, accounting for 44% of exports and 53% of imports of goods and services in 2015. When the so called "Rotterdam effect" is accounted for, the EU would still account for 41 percent of the UK's goods exports and 47 percent of goods imports.

Historically, even prior to the UK joining the EU, trade relations between the two had blossomed and consistently been on an upward trend. The percentage of UK exports going to EU15 countries was 35 percent in 1962, rising to 42 percent in 1973 as at the time of joining the EU. Between 1962 and 1973, the percentage of the UK's imports from the EU15 rose from around 30% to almost 43 percent. The positive trend was sustained and deepened after the UK joined the EU. Between 1973 and 1990, the UK export and import rates rose to about 60 percent. However, as a result of declining European competitiveness due to entrants of new participants in global trade (e.g China), there was a deep cut in the share of both imports and exports, toward the end of the 1990s. The combined effect of the global financial crisis and the persistent crisis in many euro zone countries led to a disproportionate decline in trade with EU members relative to trade with the rest of the world. However, the negative

Figure : Percentage of British exports and imports to and from the EU (1960 - 2015)



Source: Aichele and Felbermayr (2015)

3.0 Models of Post-Brexit UK trade Scenarios with the European Union and the Rest of the world

Brexit will affect most African countries primarily through the trade channels, thus the main source of apprehension for Africa remains the impact that selected exit strategies the UK adopts will have on trade interactions with the UK and the EU at large. The 2009 treaty of Lisbon gave EU member countries the opportunity to freely and unilaterally exit the EU. However, when a member elects to exit, issues relating to terms of a country's trade relations with remainder EU member states, and the means by which common policy areas are reverted to the country level are negotiated on an individual basis. It is pertinent that upon the exit of the UK from the European Union, it ceases to enjoy all the rights and privileges conferred on it by EU trade agreements. This rubs off on developing countries like Nigeria, the consequence of which will be a loss of preferential access to the UK market which EU agreements currently confer. This section discusses alternative models of potential post-Brexit options for the UK. This serves to put implications for African trade relations with the UK and the EU into perspective in light of the policy options the UK eventually adopts in exiting the European Union.

The Norwegian model

Many proponents of the UK's exit from the EU have strongly advocated the Norwegian Model be adopted and applied towards the UK Model. The Norwegian Model entails the option of the UK accessing the European Economic Area (EEA). The EEA is made up of all EU members and three non-EU members including Norway, Iceland and Liechtenstein. EEA members form part of the European Single Market, with access to unfettered movement of goods, services, people and capital. The single market refers to an integrated European economy which eliminates barriers between EU member states, predicated on the free movement of goods, people, services, and capital within the union. As part of the requirement of membership to the single market, EEA members have responsibility for the implementation of EU rules regarding the Single Market, as well as regulations with regard to consumer protection, employment, environmental and competition policy. They are however exempted from the obligation of participating in the EU's common foreign, monetary union, and security policy.

While EEA members enjoy the benefits of free trade within the EEA, they are exempted from the EU's customs union, providing them the luxury of setting their own external tariff and negotiating terms of trade with countries outside the EU. The Norwegian Model affords the UK economic benefits of an EU membership without the constraints of the perceived inconvenient marriage with the EU. Joining the EEA affords the UK the opportunity to remain a part of the Single Market while abstaining from other requirements of European integration.

The shortcomings of an EEA membership are however evident in that membership to the EU Single Market does not afford the deeper integration that occurs within the EU. Norway, for instance does not belong to the EU's customs union, implying that Norwegian exports must satisfy the requirements of the 'rules of origin' in order to enter the EU duty-free, such requirements becoming increasingly costly. According to Stewart-Brown and Bungay, (2012), the implications of these requirements include UK firms bearing part of the cost, while UK exporters have limited use of inputs imported from outside the EU to satisfy EU's rules of origin. Another downside of this option is that the EU can also use antidumping measures to restrict imports from EEA countries. According to Campos et al (2015), failure to undertake the integration pursued by EU countries would increase the cost of doing business with the EU, and lower productivity in EEA areas.

The Swiss Model

The Swiss model typifies negotiation of a series of bilateral treaties as regards relations with the EU, rather than solely being a member of the EU or the EEA. Each of the treaties makes provisions for Switzerland's participation in a particular EU policy or programme. In addition, Switzerland also maintains membership of the European Free Trade Association (EFTA), which facilitates free trade in all non-agricultural goods with the EU.

With the bilateral trade treaty option, Switzerland retains the flexibility to 'cherry pick' those EU initiatives in which it wishes to participate. The EFTA membership and an agreement covering technical barriers to trade ensure that Switzerland has a similar level of goods market integration with the EU as other EEA countries.

Switzerland does not constitute part of the Single Market for trading in services as it is yet to reach a comprehensive agreement on trade in services with the EU. Consequently, Swiss financial institutions have access to the EU market through subsidiaries in London. As the case with the EEA members, Switzerland also has no ability to shape the contents of EU programmes in which it participates, therefore unable to choose or tailor-make EU programmes to suit requirements. The Swiss model could be appealing for post-Brexit UK as it provides the 'à la carte' approach to European integration, which may satisfy desires of most Brexit proponents.

There are however significant downsides to the application of the Swiss Model to the UK. It is not guaranteed that the Swiss model would provide the same market access that EU membership offers. For example, if the UK was unable to secure participation in the Single Market in services, as was the case with Switzerland, it indicates the UK's ability to export financial and business services to the EU would be impaired. Overall, the less economic integration that the Swiss model offers will portend higher economic costs of Brexit for the UK in addition to giving up sovereignty in terms of having a say in EU decision making but would have to adopt EU legislations to be able to participate in the Single Market.

TURKISH MODEL – CUSTOMS UNION

The Turkish model entails a customs union arrangement by the UK with the EU. The custom union arrangement for Turkey is restricted to industrial goods, which ensures the elimination of all quantitative restrictions, customs duties, and other charges for these goods. Part of the custom union obligation for Turkey is the acceptance of the external tariff of the EU, known as the common external tariff (CET). Turkey is obligated to follow EU trade policy in industrial goods as a result of its sharing a common external tariff with the EU. Turkey has the ability to set its own policies, autonomous of the EU, and does not contribute to the EU budget.

The greatest challenge of a custom union arrangement for the UK is primarily evident where it relates to international trade policy. The UK will most likely under this model, have to accept the EU's external tariff even though it does not have substantial influence in shaping them. The implication of this is that the UK would allow free access to goods from countries having a Free Trade Agreement (FTA) with the EU without reciprocal access from these countries being guaranteed. This model would not allow the UK to establish its own international trade policy and would be detrimental to the UK's balance of trade.

CANADIAN MODEL

The Canadian model option for the UK's exit of the Union represents a negotiation of a free trade agreement with the EU, facilitating a free flow of goods and services between the EU and the UK. In addition, certain non-tariff and regulatory barriers would also be removed. This option differs from the Norwegian and Swiss model in that there would be no requirement for budgetary contribution or the implementation of EU laws or directives. In addition, it would not require the adoption of a common external tariff with the EU, affording the UK freedom to implement an independent international trade policy, similar in this respect to the Turkey customs union.

The shortcomings associated with this option are the restrictive effects of a UK-EU Free Trade Agreement (FTA), as this only provides for free movements of goods and services, while restricting the flow of capital and/or labour. The well-developed UK financial market will therefore, not benefit from an FTA arrangement with the EU. Furthermore, the substantial time taken for typical FTA negotiations to consummate may heighten and prolong the uncertainty associated with Brexit, the effects of which may be destructive to financial markets in Europe and frontier economies.

AUSTRALIAN MODEL – NO PREFERENTIAL ACCESS

The Australian Model represents the default scenario, as it involves the UK completely walking away from the EU - an exit agreement that severs any further formal relationship. In this scenario, trade relations between the EU and the UK would be covered by World Trade Organisation (WTO rules) which applies to all members' international trade relations. The rules provide for no free movement or financial contribution and no obligation to apply EU laws. However, traded goods would have to meet EU standards.

4.0 BREXIT and the Nigerian Economy

There is no gainsaying the fact that shocks to the British economy, the kind that Brexit typifies, will have profound effects on the global economy, both in the short and long run horizons. The British economy is estimated to be worth about $3 trillion, ranking second largest economy within the EU and the fifth globally. This fact is exemplified in the immediate response of global and domestic financial markets to the news of Brexit. On 24 June, global stocks lost USD2 trillion in value, with banks in the UK being among the most affected, as USD55 billion was wiped off banking stocks. Nigerian stocks fell by 1.4%, reversing a rally of 8.5% in the week preceding Brexit, with at least two Nigerian banks recording the greatest losses.

Besides the immediate market reactions, it is expected in the medium term, that a number of disruptive effects of Brexit on the UK's political and social economic landscape may manifest. There is the possibility of heightened political tension as there are presently talks of additional referenda within the UK with Scotland and Northern Ireland planning their exit from the UK in order to retain EU membership. Within the EU, Brexit may precipitate further exits of EU member states (Italy, etc.), although final exit is not expected to take place for at least two years. Britain is expected to activate Article 50 of the Lisbon Treaty, which establishes the procedures for a member state to withdraw from the EU but barring this, a speculative reaction by savvy investors has already spurred a currency flight from the British Pound to the US Dollar and Gold. It remains the responsibility of monetary and fiscal authorities to stem this trend by reassuring the markets and setting up fresh trade agreements with EU member states to maintain existing relationships and calm markets tensions.

The exit will precipitate widening regulatory divergence, increasing the cost of trade, impacting on volumes and UK supply chains. The swift diminution in the value of the Pound has reduced the net worth of UK based entities as well as their purchasing power. The UK will painfully face the reality of losing to other locations within the EU, the epicentre of corporate finance and its position as a base for most leading corporate headquarters. It may also bear the negative consequence of losing its appeal as an investment capital hub in the European region and as a gateway to the rest of Europe.

By virtue of being a former British colony, Nigeria has an extensive trade cooperation with the UK which dates back several decades, and an estimated USD8.3 billion worth of bilateral trade recorded between the two countries. This is projected to reach USD25 billion by 2020 as remittances to Nigeria from the UK averaged USD21 billion a year. In addition to being Nigeria's largest source of foreign investment, with assets worth over USD1.4 billion, the UK is also one of the largest donors to developmental assistance in Nigeria.

The fortunes of the Nigerian banking system are inextricably tied to the overall well-being of the wider macroeconomic environment in which it operates.

Hence, the effects of Brexit on the banking industry will be derived from a wider assessment of the impact of the on the Nigerian economy through various channels, including but not limited to the financial markets, trade, remittances etc.

For Nigeria, Brexit has coincided with a time the nation is faced with constraining external and internal economic challenges. As it were, Brexit portends grave implications which may aggravate present dire economic circumstances; while at the same time providing prospects and opportunities which may be levied upon given appropriate and proactive actions on the part of economic policy making. The rest of this section analyses the effects of the yet unfolding scenario on the Nigerian economy at large, while further highlighting how it affects the Nigerian banking industry in particular.

4.1 Implications of Brexit on the Nigerian Economy

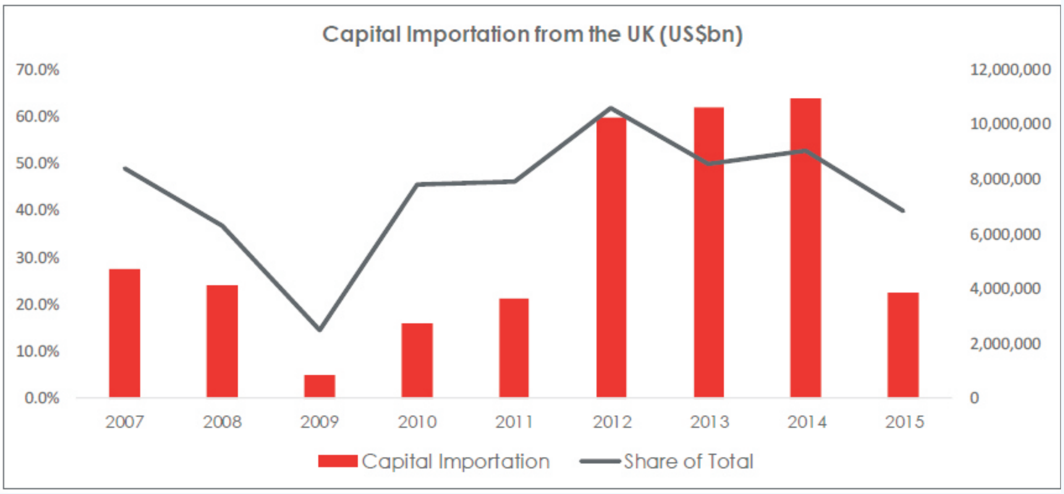
Uncertainty-induced financial markets turmoil: The short-term impacts of Brexit stem mainly from the uncertainty that the Brexit vote has caused. Financial market participants are faced with unclear scenarios on the nature of the new relationship between the UK and the EU - uncertainty which will likely persist for the next two and half years. This uncertainty is currently reverberating in the nation's currency and stock markets. The Nigerian Stock Exchange took a dramatic turn from successive weeks' rally to shed 1.4 percent on the announcement of the Brexit outcome, and to date, the market is yet to recover from the negative sentiments. The fact that Nigeria floated its currency a week before the Brexit vote, had far-reaching impacts as it has since remained a mirage for the Naira to find its new equilibrium relative to the dollar. While local factors have also been at play, experts have implicated the increased risk aversion towards Pounds-denominated assets as the cause of invigoration and strengthening of the dollar globally. Another veritable source of uncertainty is the possible scrapping of EU law which could result in an avalanche of new legislation in the UK. This could accentuate volatility in global financial markets and with an ensuing contagion effect on the erstwhile fragile Nigerian financial market.

Capital flows: Brexit has precipitated an unprecedented instability in the UK economy; going forward, experts have projected a weaker and slower UK economy. Prospects are high for a 'flight to safety' from the UK and the entire European Union. With the foregoing, financial conditions in Europe are expected to remain largely restricted. The UK accounted for an average of 44% of capital importation to Nigeria over the last five years (Figure 2). Tight credit conditions will dampen cross-border bank lending and bond issuances, presenting a significant threat to Nigeria's plan to issue Euro bonds to cover gaps in fiscal balances. Nigerian banks have high exposure to credit lines originating in the Euro area, and strengthening of the US dollar post-Brexit, could further raise the cost of servicing these facilities. These conditions do not bode well for the currently fragile financial and banking systems in Nigeria, heightening the risk of further credit rating downgrades.

Breakfast Session on BREXIT and its Implications on the Nigerian Banking Industry

July 1, 2016

Figure : Capital Importation from the UK (2007 -2015) (US$Bn)



Source: United Capital Research

Trade: Nigeria's trade with the UK is currently estimated at US$8.3 billion and is projected to reach US$26 billion in 2020. Data available from the NBS revealed that the UK accounted for 4.2 per cent (or N284bn) of total imports to Nigeria in 2015 compared to 6.6 per cent (or N370bn) in 2012. Similarly, the UK accounted for 4.3 per cent (or N415bn) of total exports from Nigeria in 2015 compared to 6.6 per cent (or N1.5trn) in 2012.

Table 2: Total Import Trade between Nigeria, EU and UK, from 2012-2015

	Total Imports (N' Million)				
	Total Imports to Nigeria	Europe	UK	% of Total Imports to Nigeria from UK	% of EU Imports to Nigeria from UK
2012	5,624,870.40	1,490,398.00	370,157.70	6.60%	24.80%
2013	7,015,814.70	2,376,232.10	367,066.40	5.20%	15.40%
2014	7,374,370.50	2,693,980.40	289,289.80	3.90%	10.70%
2015	6,697,965.90	2,501,649.40	283,759.20	4.20%	11.30%

Source: National Bureau of Statistics

Table 3: Nigeria's Export Trade to the EU and UK, 2012-2015

	Total Exports (N' Million)				
	Total Exports from Nigeria	Europe	UK	% of Total Exports to Nigeria from UK	% of EU Exports to Nigeria from UK
2012	22,446,320.23	8,227,089.70	1,480,800.30	6.60%	18.00%
2013	14,245,271.60	6,079,150.50	729,939.00	5.10%	12.00%
2014	16,304,041.20	6,881,169.90	824,918.80	5.10%	12.00%
2015	9,593,042.00	3,812,573.30	414,846.40	4.30%	10.90%

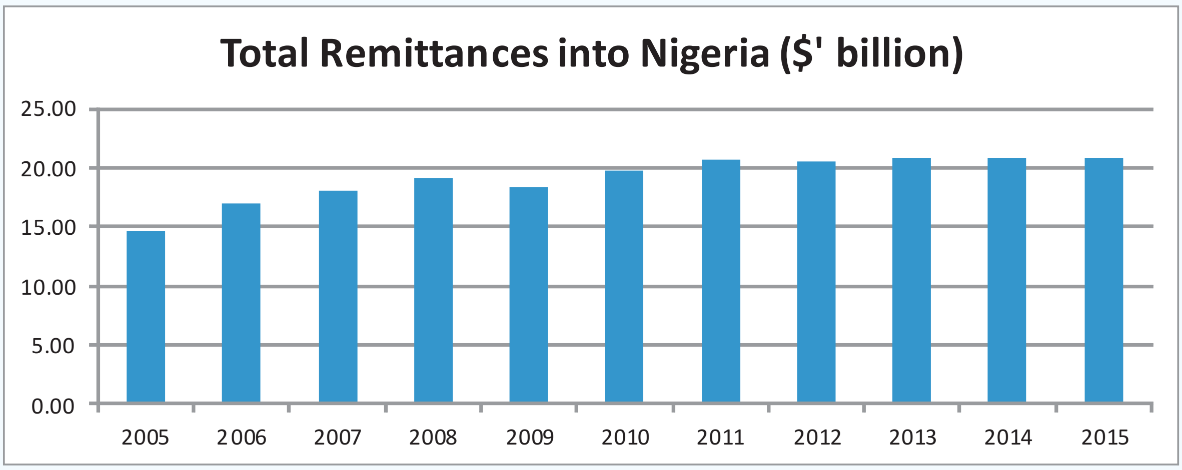
Source: National Bureau of Statistics

Brexit portends substantial disruption to trade agreements subsisting under the auspices of the EU. As these agreements are being renegotiated, and depending on the exit route the UK eventually adopts, a weakening of trade between the UK and the EU is inevitable. The possible loss of the UK's access to the EU's single market may force a negotiation of new trade agreements with regional economic blocks and strong trade ties with the UK, such as the Economic Community of West African States (ECOWAS), the biggest EU trading partner in Africa, and bilateral trade agreements with Nigeria. Trade with the EU on the other hand could suffer the impact of Brexit, and is generally destined to weaken while these renegotiations last. Currently, discussions on the signing of an Economic Partnership Agreement (EPA) with the EU holds prospects for preferential trades with the EU for Nigeria and other countries in the regional bloc. The Brexit move may cause a delay in the signing of this agreement which could negatively affect trade balance in Nigeria.

Scale-Down on Investment and Aid Donation to Nigeria: A weaker and smaller UK economy is expected to scale back its aid donation and investment in development projects in Nigeria, as with the European Union. In Nigeria, for instance, the UK Department for International Development (DFID) had a portfolio of 40 projects with a planned budget of £232 million for 2014 -2015. In addition, the contribution the UK makes to the World Bank makes its total investment up to about £400 million a year in development aid to Nigeria.

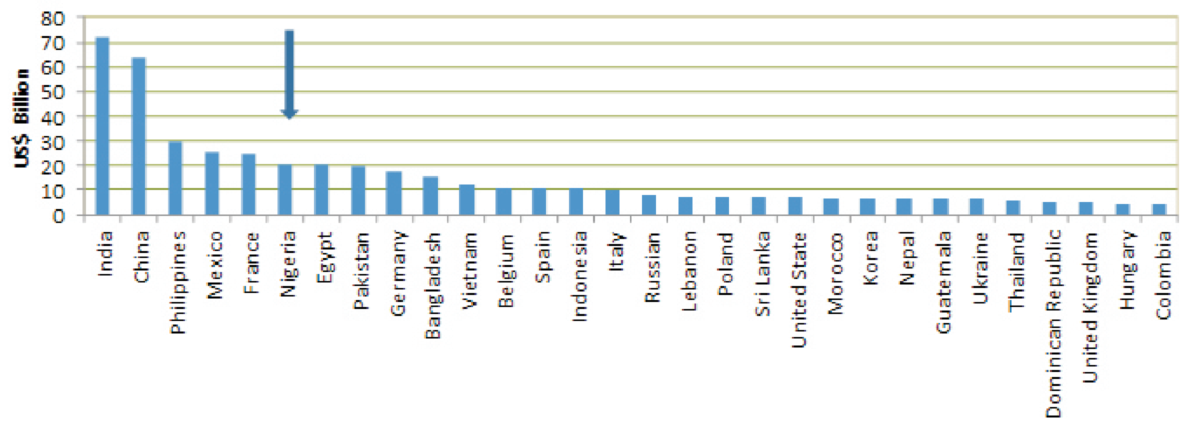
Migration and Remittances: Tougher stance on immigration issues remains one of the strongest sentiments underlying the Brexit vote. As such, post-Brexit UK may impose stricter regulations on immigration to the UK. Presently, Nigeria has over one million of her citizens in the United Kingdom, likely to suffer the consequences of harsh immigration regulations which may be implemented. In addition, Nigeria is the most remittance-dependent country in Sub Sahara Africa, and a decline or stagnation in migrants' remittances from the UK and the EU could intensify Nigeria's liquidity challenges. With remittances from the Nigerian diaspora in the UK amounting to $21 billion on annual average, the devaluation of the pound means a diminution of this important development finance alternative for Nigeria.

Figure 3: Total Remittances into Nigeria, 2005-2015



Source: World Bank

Figure 4: Top Remittances of Receiving Countries in the World (2015, US$ Billion)



4.2 Implications of Brexit on Nigerian Banking System

Due to the bilateral relationship that exists between Nigeria and the United Kingdom (the financial hub of the Euro area); an aftermath of the Brexit is likely to present a ripple effect on countries such as Nigeria, highly dependent on the UK in the areas of trade and finance. As Nigerian banks have branches and subsidiaries across the EU, the repercussion of policy changes may be spilled over to the banking sector through "Cross banking Activities/operations". Developments and changes to the EU banking sector may also have a triggered effect on Nigeria's Domestic banks. The following are likely developments that may arise in the Banking and financial sector:

Effect on Cross-Border Banking Activities/Operations

The Nigerian financial system is comprised of numerous banks operating branches and subsidiaries in African and European countries, far exceeding that of foreign banks operating in Nigeria. The parent companies with subsidiaries mainly benefit from increased profits and diversification. The recipient banking system through improved intermediation, effective and efficient technological advancement, and increased profit also stand to benefit.

Table 1: List of banks' branches/subsidiaries/Rep offices:

S/N	BANK	LOCATION OF OFFSHORE BRANCHES			TOTAL
		WEST AFRICA	OTHER AFRICAN COUNTRIES	OUTSIDE AFRICA (EURO AREA)	
1.	Access bank	3	4	2	9
2.	Main Stream bank	-	-	1	1
3.	Diamond Bank	4	-	1	5
4.	FCMB bank	1	1	1	3
5.	First Bank of Nigeria	5	2	3	10
6.	Guarantee Trust Bank	5	3	2	10
7.	Key Stone bank	3	1	-	4
8.	Skye bank	3	-	-	3
9.	United Bank for Africa	9	10	2	21
10.	Union Bank	1	1	1	3
11.	Zenith	3	1	1	5
	Total	37	23	14	74

Source: BSD, Central Bank of Nigeria

Nigerian Banks have branches and subsidiaries spread across the United Kingdom (UK) and 27 EU member countries. Based on recent developments, there may be rising concerns over granting new licenses to Nigerian Banks by the UK or the EU banking authorities. There is also the issue of relocating central euro clearing activities; from London to Frankfurt or Paris. The developments however create new expenses in contingency planning and, potentially for relocation of cross banking activities. It is envisaged that at the longer term, the cost of relocation from London to the "new hub" due to Brexit could be reduced for the sister banks operating abroad.

Brexit is expected to reduce the number of bank staff working in London and could accelerate plans to shift some operations to cheaper locations; some banks operating there may have begun the process. Financial Analyst, Mike Mayo envisaged that 'at the longer-term, some US banks could potentially benefit from Brexit given the high operation costs in London,' adding that some functions may be duplicated in London and in the EU, thereby reducing savings.

In terms of investment banking, an initial vote to remain in the EU was projected to increase corporate activities and bank profits. Given the final stand on the exit, however, investment banking activities are expected to dampen and may greatly reduce the velocity of deals and transactions by some percentage, thus reducing their banks profits.

Interest Rates to remain lowered for longer period

Analysts have envisaged, prior to the exit, that interest rates would be heightened by either the Federal Reserve or the European Central Bank, although not in the nearest term. In the aftermath of the Brexit vote, analysts from RBC have observed that rates would remain "static through the second half of 2016 and most of the periods in 2017 due to the level of uncertainty and fragility". Banks inevitably record lower profit when interest rates are low, as the gap between payments for funding and loan charges narrow. This may affect the general performance of both subsidiary and domestic banks (Banks operating in Nigeria). As a fall-out of the Brexit vote, most UK banks' subsidiaries and branches have cut their profit forecasts. For instance, Morgan Stanley cut its 2018 earnings forecasts for its UK subsidiaries by 12 to 27 per cent due to "macro implications" of the Brexit vote. The impact is expected to manifest in two folds: lower loan growth as the economy slows, and higher loan losses.

4.3 Brexit and the Opportunities for Nigeria

In spite of looming challenges posed by Brexit for Nigeria, there are opportunities to be maximised. The British pound is currently at an all-time low due to short term panic from Brexit, nonetheless, the British's estimated US$3 trillion economy is still robust and resilient. In the short term, this provides a once in a life time opportunity for Nigerian banks to make huge investments in UK financial assets. For other savvy investors, investment in the UK real estate and hospitality sectors may be lucrative considering the exceptionally weak pound sterling. The weakening of the British pound provides prospects for improved trade competitiveness for Nigerian exports. The persistent weakening of the Naira in the new flexible exchange rate regime, on the other hand, may obviate this opportunity.

Brexit affords the UK leeway to explore new opportunities and new markets. Nigeria's commodities and solid minerals markets may potentially become ready alternatives to the diminishing trading opportunities between the UK and EU. One of the highpoints of the proponents of Brexit is the fact that the EU's Common Agricultural Policy (CAP) is not beneficial to the UK, a net importer of agricultural products. Hitherto, CAP has restrained African farmers' access to European markets. Whereas with Brexit, prospects are high for the UK to develop its own agricultural trade policy from which African farmers stand to benefit from improved access to the UK market, thereby boosting competitiveness.

In addition, Nigeria may leverage on the Brexit opportunity for direct negotiations with the UK and activate favorable trade relations, previously moribund due to multilateral negotiations. More importantly, there is a need for Nigeria, particularly the Central Bank of Nigeria, to develop robust strategies for mitigating the adverse effects and risks that may emanate from the development. One such way is ther oll-out of viable measures to attract foreign portfolio investment (FPI) for reserve accretion.

5.0 Conclusion

The UK exited the European Union at a time Nigeria, as with many other African countries, grapples with acute internal imbalance and external shocks occasioned by easing commodity prices and economic slowdowns in other major industrial economies. Notwithstanding, Brexit has presented opportunities and challenges for Nigeria, and while precise quantification of these currently remain a challenge, aggregates of probable consequences indicate undesired effects on the banking system and the economy at large. While developments from the external fronts may be outside the purview of domestic economic policy, timely and proactive policies that stimulate the domestic economy in order to minimize the negative impacts of Brexit remain a priority.

References:

Cameron, D. (2013) 'EU Speech at Bloomberg', 23 January 2013. Retrieved from: https://www.gov.uk/government/speeches/eu-speech-at-bloomberg

Campos, N., F. Coricelli and L. Moretti. (2015) 'Norwegian Rhapsody? The Political Economy Benefits of Regional Integration', CEPR Discussion Paper 10653.

Financial Times, (July 4, 2016) "The 9 Ways Brexit Will Affect Foreign Banks".

Financial Times, (July 2016) "Will Foreign Banks Leave the Uk after Brexit"

Aichele, R; Felbermayr, G. & Heiland, I. (2015); "Costs and benefits of a United Kingdom exit from the European Union," Center for International Economics, Munich. Retrieved from: https://www.bertelsmann-tiftung.de/fileadmin/files/BSt/Publikationen/GrauePublikationen/BREXIT_EN.pdf.

BREAKFAST SESSION ON THE IMPLICATIONS OF BREXIT ON THE NIGERIAN BANKING INDUSTRY

HELD ON FRIDAY, JULY 1, 2016 AT THE BANKERS HOUSE, VICTORIA ISLAND, LAGOS

COMMUNIQUE

The Chartered Institute of Bankers of Nigeria Centre for Financial Studies (CIBNCFS), a subsidiary of The Chartered Institute of Bankers of Nigeria, organized a Breakfast Session on Implications of BREXIT on the Nigerian Banking Industry. The Session was held on Friday, July 1, 2016 at the Bankers House, Victoria Island, Lagos. A total of 112 (One hundred and twelve) participants drawn from Regulatory Institutions, Deposit Money Banks (DMBs), Tertiary Institutions, Microfinance Institutions, Oil and Gas Companies, Multinational Companies and the Diplomatic Community were present.

The objective of the Session was to x-ray the implications of the recently announced exit of the United Kingdom from the European Union on the banking industry in particular and the Nigerian economy in general and discuss opportunities to be leveraged on for improved business performance.

The following are the highlights of the Session:

1. **The Significance of the UK**
   This is premised on certain fundamental issues which include:

- The historical relevance of UK in the Comity of nations.
- Most legal, economic, socio-cultural and commercial structures globally trace their origin to UK.
- The UK occupies a central position in global trade, politics and economic alignment
- Most Commonwealth countries still look up to UK for leadership and direction.

2. **General Implications of BREXIT**
   Some global, social, political and economic considerations of BREXIT include

- Its implications on diplomatic relations.
- The possibility of Scotland and Ireland redefining their status as part of Great Britain.
- BREXIT was a shock to the world and has created a lot of uncertainties in the global economy. It suggested a seismic shift from regulatory authorities' ability to wield power to decision making by the people.
- The uncertainties would affect business performances, capital formation, asset value in terms of stocks and real estate, consumers and investors' confidence and consumers' purchasing power.
- The probable recession would not only be a UK recession but a European Union wide recession which, due to globalization and contagion effect, would be felt globally.
- The role of UK as the global financial centre could be altered with the resultant negative impact of BREXIT on Small and Medium Enterprises' (SMEs) ability to access cheap funds.
- It is likely that there would be a shift of trade and other transaction destinations away from the UK.
- Euro clearing presently in the UK is likely to move to another country in Europe. This would significantly impact banks as it would imply a two-way clearing instead of the initial one-way system. In other words, a UK clearing and the Euro clearing systems.
- The long-term impacts of BREXIT would only be a forecast as no one can accurately dimension them.
- BREXIT has produced immense political chaos such as the crisis of how to initiate Article 50; crisis of Prime Minister David Cameron's resignation; crisis of handling the tons of legislations needed to achieve the full implementation of BREXIT; crisis of the contagion effects of BREXIT on political decisions in other countries.
- BREXIT does not spell doom if the UK could strategically negotiate with the other European Union countries.
- The outcome of the referendum might have been different if voters were adequately equipped with the right information.

3. **Implications of BREXIT on Nigeria and Nigerian Banks**

For Nigerian banks, BREXIT throws open a number of pressing issues such as;

- Lending and borrowing as well as Correspondent banking relationships entered into under the aegis of Europe.
- The impact on assets and liabilities in GBP and the Euro given the possibility of depreciation and appreciation in those currencies.
- Treatment to be given to the differentials in currency values in the books of banks under the IFRS.
- Impact on banks' open position as designated in those currencies.
- Impact on bank customers whose deposits and assets are in affected currencies.
- Futures transactions in Euro and GBP.
- BREXIT could imply a smaller United Kingdom and reduce the UK's capacity to absorb Nigeria's export which currently stands at 5.9%.
- A smaller UK economy would also imply a significant reduction in the credit lines currently enjoyed by Nigeria.
- Remittances to Nigeria by its citizens in the UK will decrease significantly. According to an European Union report, the number of Nigerian professionals working in the European Union is more than the number of Nigerian professionals working within its shores. Nigerians sent home $20 billion worth of remittances in 2015.
- The Uk is currently Nigeria's largest source of foreign investment with assets worth over $1.4billion dollars earned in 2015. The event of BREXIT could affect the value of these assets
- Bilateral trade between Nigeria and the UK currently valued at £6 billion and projected to reach £20 billion by 2030 could be affected.

4. **Lessons and Recommendations**

- BREXIT has shown that there is the need for Nigeria to proactively diversify its export destinations and products in order to be able to absorb shocks from the international market.
- The banking industry would need to intensify efforts at sourcing credit lines outside of the UK and develop products and services that would appeal to the retail market.
- The Nigerian Government should brace itself to addressing the likelihood of an influx of Nigerians in the Diaspora to the country thereby exacerbating the currently high level of unemployment in the country. Presently, major banks in the UK are announcing job losses.
- To forestall possible contagion effect, Nigeria should take steps to mitigate the current UK's "cutting off" of the country as a result of the country's low economic performance in the last 18 months by looking at alternative business channels and lines.
- There is the need for Nigeria to develop a robust Risk Assessment Framework in the face of BREXIT. The Central Bank of Nigeria should, as a matter of urgency, intensify the current efforts at carrying out a proper risk diagnosis of BREXIT.
- The CIBN should expand the scope of and regualrly update the content of its capacity building efforts like the Compulsory Continous Development Programmes (CCPD) as a direct response to the expected developments from the effects of BREXIT.
- Political and corporate leaders should exhibit the highest levels of discipline in the management of resources which they hold in trust.

BUSINESS DYNAMICS UNDER A FLEXIBLE EXCHANGE RATE REGIME

Being the Welcome Remarks by the President and Chairman of Council at the Breakfast Session on the above Theme on Friday, July 15, 2016

Ladies and gentlemen

The interaction between business management and exchange rate is very profound especially in developing economies such as Nigeria where heavy reliance is placed on imported basic necessities of life. This is so because the array of imported items covers:

-consumer durable and non-durables,

-heavy industrial plant and machinery,

-manpower and technology.

Hence, most businesses operating in such countries depend on a friendly exchange rate regime to survive and/or operate profitably.

The challenges inherent in the structure of our economy begin with the near impossibility of the market system to operate without interference. Market system ensures efficient distributive system when the forces of demand and supply are allowed to operate unfettered.

Ladies and gentlemen, market distortions are prevalent all through history. From the labor market to financial market down to the commodity market, governments often have genuine political reasons to intervene, usually to seek the greater good of the greater number.

Foreign exchange as a commodity is not insulated from this intervention. Indeed, from the pre industrial revolution to this present age, the global search for a workable, efficient and fair exchange rate regime continues unabated.

-The Bretton Woods Agreement of 1945 and the birth of some international financial institutions were products of the search.

-The evolvement of the gold standard, gold exchange standard, dollar standard, flexible, adjustable pegged regimes have all been attempts at finding a just allocative system to minimize on one part notable distributive injustice.

Nigeria is known to have tried almost every conceivable foreign exchange allocative system and the search for a more acceptable system still continues.

Let me remind us that our own situation is this complex because when wages are indexed to the dollar, about 70% of Nigerians are said to be living on less than two dollars a day. The prevalence of poverty is therefore a daunting challenge to a government that is desirous to promote economic welfare.

How then can this be done if market forces are allowed to dictate exchange rate when the propensity of the citizenry to consume imported commodities is still abnormally high?

In situations like this, the call for either high subsidy or tax to redress observed distributive injustice often reaches the roof top, breeding unfortunately rent seeking individuals and corruption in high places.

The flexible exchange rate is therefore another attempt at finding a workable exchange rate regime in Nigeria and for Nigerians. The underlying facts are well known. In a situation where there are supply rigidities, attempts to administratively regulate prices promote black marketeering. Herein lies the challenge of the Authorities. Should the Naira be allowed to float freely? Some have argued that pegging the exchange rate at about N270 to a dollar is equally unrealistic.

Whatever view is held, the immediate implications of the flexible exchange rate regime on businesses of all types and at all levels are:

-increase in cost of factor inputs, hence cost of production.

However, with at best stagnated wages, low productivity, fall in real income due to inflation and increasing level of unemployment, the capacity of consumers to absorb further increases in commodity prices is limited.

Accordingly, total demand may fall, leading to reduced output, stunted growth and reversed development and eventually fall in both nominal and real GDP.

Businesses have to redefine their dynamics. It happened before when in the 1980s and 1990s flour millers and breweries, among others, moved away from wheat technology to locally grown sorghum and corn, to cassava bread, etc. That eventually reduced their exposure to the scarce, expensive foreign exchange.

More than before, businesses need to redefine focus, move away from import dependent technology and substitute imported raw materials for local ones. Consumers need to buy into the new dynamics and tame their insatiable appetite for imported commodities. Government should provide more incentives for businesses that succeed in their quest for import substitution and export promotion.

The CBN has done well by allowing the market to play a role in determining exchange rate for the Naira, to promote allocative efficiency. If businesses can reorder their modus operandi as counseled above, Nigeria's economy and Nigerians stand to be the gainers.

I welcome you all to this Breakfast Session.

Professor Segun Ajibola, Ph.D, FCIB

President/Chairman of Council
The Chartered Institute of Bankers of Nigeria

BREAKFAST SESSION ON BUSINESS DYNAMICS UNDER A FLEXIBLE EXCHANGE RATE REGIME

Date: July 15, 2016

BREAKFAST SESSION ON

BUSINESS DYNAMICS UNDER A FLEXIBLE EXCHANGE RATE REGIME

HELD ON FRIDAY, JULY 15, 2016 AT THE BANKERS HOUSE, VICTORIA ISLAND, LAGOS

COMMUNIQUE

The Chartered Institute of Bankers of Nigeria Centre for Financial Studies (CIBNCFS), a subsidiary of The Chartered Institute of Bankers of Nigeria, organized a Breakfast Session on Business Dynamics Under a Flexible Exchange Rate Regime. The Session was held on Friday, July 15, 2016 at the Bankers House, Victoria Island, Lagos. Bankers House, Victoria Island, Lagos. A total of 37 (Thirty-Seven) participants drawn from the Central Bank of Nigeria (CBN), Deposit Money Banks (DMBs) and the Telecommunications industry were in attendance.

The objective of the Session was to x-ray the newly introduced flexible exchange rate regime by the Central Bank of Nigeria on the country's business environment and peculiarities vis-à-vis other successful countries' examples under a similar regime. This was done with a view to leveraging on their experiences for improved business performance and growth of the nation.
The following are the highlights of the Session:

Reasons for the Introduction of the Flexible Exchange Rate

In mid-2014 the price of crude oil declined from $110 to $27 per barrel. This caused a decline in foreign reserves leading to restrictions and rationing. The Government through the CBN introduced policies to address the resulting negative effects on the economy.

There were higher likelihoods of abuse and corruption in the last exchange rate regim

The floating exchange rate system would be more transparent because it is determined by market forces

The reduction in the major source of reserves derived from the downstream sector among other things led to the widespread uncertainties in the country. The Government needed to tackle the uncertainties and therefore introduced the flexible exchange rate regime. The new regime is expected to stabilize the foreign exchange market as prices would be determined by the forces of demand and supply.

The flexible exchange rate has brought about a sense of security because it calls for greater efficiency in the management of scarce foreign reserves. Since the value of the Naira has fallen under this exchange rate regime, a higher amount of foreign exchange is required to pay for imports. Nigeria is now forced to look toward locally produced or import substituted products in an attempt to save its residual foreign reserves.
Some of the Issues Raised by Participants on the New Flexible Foreign Exchange

How liberal is the new foreign rate exchange policy? Under a flexible exchange rate regime there should only be a single market for foreign exchange determined by the forces of demand and supply. This is currently not the case in Nigeria as there are still parallel markets and a significant gap between them. This means that there are still opportunities for arbitrage and rent seeking.

How do we control transactions which are not eligible to have access to Forex as stated in the Central Bank of Nigeria's Guidelines? Traders who demand foreign currency for unauthorized transactions (such as importing toothpicks) would be forced to source for funds from the black market. Traders who have been importing banned items for decades may not stop even after restrictions have been made. These traders would instead seek foreign exchange from the black market to carry out their transactions since there are still parallel markets.

The eligibility to operate as an Authorized Foreign Exchange Dealer must be monitored closely to avoid abuse

There is a cloud of uncertainty regarding the effectiveness of this new exchange rate policy. A couple of months after this regime was introduced, investors are still fleeing Nigeria while production has decreased and inflation rates are at an all-time high.

There is widespread insecurity across Nigeria which has disrupted normal economic activities. For example, the activities of the militants in the Niger Delta, has disrupted crude oil production. Oil production in Angola has now surpassed that of Nigeria.

The new exchange rate regime has caused a "Catch 22" dilemma. This is because, while we do not have enough foreign reserves to sustain the previous fixed exchange rate, the new floating exchange rate presents challenges of a persistent increase in costs.

Implications of the Floating Exchange Rate Regime

Since the introduction of the new exchange rate regime, there has been a direct increase in costs without a corresponding increase in income. Likewise, purchasing power of the average Nigerian has reduced significantly.

The price of oil recently increased to $50 per barrel but Nigeria could not take advantage of this price hike because we are not producing at full capacity.

Issues of backlogs and debt financing in the downstream sector are yet to be resolved. Dollar denominated loans and security instruments generated in the previous exchange regime have been affected as the value of the Naira to the Dollar has been adjusted.

Authorized Foreign Exchange Dealers may be discouraged from patronizing the official rate due to arbitrage gains to be earned in the black market

The current exchange rate regime needs more capital to operate on the same level as it was in the fixed exchange rate regime.

Recommendations

The Government needs to restore peace to the Niger Delta and other conflict affected parts of Nigeria so that production of crude oil and other economic activities operate at their full capacities.

The Government needs to implement more import substitution and export promotion policies. This could be done by reducing the amount of bottlenecks in the system affecting potential exporters. In countries like Kenya and Ghana, the locals have the capacity to produce quality products due to their collaborative relationships with the governments.

We must increase our competitive capacity. The quality of Nigerian exports must improve if foreigners are to patronize our products and services. This would positively affect foreign exchange earnings.

CBN should clear the backlogs of foreign exchange debts so as to prevent systemic loss.

The Government should provide incentives for businesses who succeed in their quest to provide more import substituted products as well as export promoted products.

· Nigeria needs to regain the confidence of investors and trading partners. Nigeria's credit worthiness is questionable to the international community and must be improved upon.

·

The CBN should encourage the developments of more products whose payments can be deferred (forward contract).

The Government should create an enabling business environment by encouraging transparent incentives that would attract Nigerians in the Diaspora to come and invest in the country. This would also attract Foreign Direct Investments (FDIs) from friends of Nigerians in the Diaspora.

The Government should put in place an operative Securities and Commodity Exchange Board.

The Government should encourage the establishment of the Nigerian Financial Centre and create more Export Processing and Free Trade Zones.

The quality of made-in-Nigeria goods should be improved to encourage local consumption.

The Government should develop programmes for the SMEs that would not only provide them with the needed funds but also with the attendant technical support to efficiently manage the funds.

There is also the need for an AMCON type of structure for the SMEs as a safety net for them.

Authorized dealers must be scrutinized before they are offered licenses to operate.